Supreme Court, U.S.
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Nos. 01-950, 01-1018

IN THE

Supreme Court of the United States

HILLSIDE DAIRY, INC., A&A DAIRY, L&S DAIRY, AND MILKY WAY FARMS,

Petitioners,

and

PONDEROSA DAIRY, PAHRUMP DAIRY, ROCKVIEW DAIRIES, INC., AND DARREL KUIPER AND DIANE KUIPER, D/B/A D. KUIPER DAIRY,

Petitioners,

v.

WILLIAM J. LYONS, JR., SECRETARY, DEPARTMENT OF FOOD & AGRICULTURE, STATE OF CALIFORNIA, AND ROBERT TAD BELL, UNDERSECRETARY, DEPARTMENT OF FOOD & AGRICULTURE, STATE OF CALIFORNIA,

Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR WESTERN UNITED DAIRYMEN AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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QUESTIONS PRESENTED

1. Whether the exemption granted by 7 U.S.C. § 7254 extends to California's pricing and pooling regulations; and

2. Whether an individual can state a claim for a violation of the Privileges and Immunities Clause where a state law distinguishes on its face upon whether a farm is located in-state or out-of-state and not between the "residency" or "citizenship" of the individuals that own or operate the farm.

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STATEMENT OF INTERESTS OF *AMICUS CURIAE*

Western United Dairymen is a non-profit trade association.[1] Its members are dairy farmers (producers) throughout California, from the Oregon to the Mexican borders. It members comprise approximately 1,100 of California's 1,900 total dairy producers. Many of its members hold varying amounts of quota[2] allotments under California's Milk Pooling Plan and many do not hold any quota. Western United Dairymen's members are vitally interested in and directly affected by the Milk Pooling Plan as their livelihoods are related, in large part, to its operation. The parties' written consents to Western United Dairymen's filing of an *amicus curiae* brief in support of Respondents are being lodged herewith.

STATEMENT OF FACTS

California uses a system of three interrelated programs to regulate milk that is produced, processed or sold in California. The Milk and Milk Products Act of 1947, Cal. Food & Agric. Code, §§ 32501-39912, and the regulations promulgated thereunder, establish standards for the composition of milk, including fluid milk. The Stabilization and Marketing Act, Cal. Food & Agric. Code, §§ 61801-62403, and the Stabilization and Marketing Plans established thereunder, set minimum classified prices to be paid for raw milk based upon the use to which the milk was put. The Gonsalves Milk Pooling Act, Cal. Food & Agric. Code §§ 62700-62756, and the Pooling Plan promulgated thereunder[3], implemented blended prices to

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1. No person or entity other than Western United Dairymen, its members, or its counsel, have made a monetary contribution to the preparation or submission of this brief, and this brief is authored entirely by counsel for the Western United Dairymen and counsel for a party did not author any part of this brief.

2. "Quota" is explained on pages 4 through 5, *infra*, and Appendix C, section A.

3. The current version of the Pooling Plan is available at *http://www.cdfa.ca.gov/mkt/mp/poolplan.pdf*.

California dairy farmers, also referred to as producers[4], and a producer pool equalization system. The Stabilization and Marketing Act and the Milk Pooling Act, and their respective Plans, together constitute the pricing and pooling component of California's integrated milk regulation system.

California's milk pricing and pooling system exists alongside a parallel Federal milk pricing and pooling system, established by the Agricultural Adjustment Act, reenacted by the Agricultural Marketing Agreement Act of 1937, 7 U.S.C. § 601 *et seq.* (hereinafter, the "Federal Marketing Act"), pursuant to which the U.S. Secretary of Agriculture may issue regional milk pricing regulations, referred to as "Federal Milk Marketing Orders", at the request of milk processors and/or producers within a marketing area. *See* 7 U.S.C. § 608c. As discussed, *infra*, California has the right to maintain, with the assent of its producers, its own state program and is not compelled to be a part of the Federal Milk Marketing Order system. Indeed, several areas of the United States, including California, have declined to be governed by Federal Milk Marketing Orders. *See* Appendix A, a map of the 11 current Federal Milk Marketing Orders established pursuant to 7 U.S.C. § 7255. Both California and the Federal government instituted their respective pricing systems to curb destructive trade practices that had developed in the dairy industry. *See, e.g., Lehigh Valley Cooperative Farmers, Inc. v. United States*, 370 U.S. 76, 79 (1962).

A. The California Stabilization and Marketing Act and Classified Minimum Pricing.

Since 1935, when it enacted the Young Act, California has set the minimum prices that milk processors must pay to California producers for raw milk. *See* Cal. Stats. 1935, c. 241

4. As used herein, the terms "California producer" or "California farmer" refer to milk production facilities, i.e. dairy farms, located within the State of California, regardless of the residence or citizenship of the entities or individuals operating or owning the farm. The term "in-state milk" refers to milk produced at a farm located in California, regardless of the residence or citizenship of the entities or individuals operating or owning the farm. "Out-of-state milk" refers to milk produced at a farm located outside of California, regardless of the residence or citizenship of the entities or individuals operating or owning the farm.

§ 1. The California Legislature adopted minimum pricing laws to stabilize the chaotic and abusive market conditions that previously existed in California's dairy industry. These conditions existed, in large part, because milk is produced daily, is perishable and must be marketed virtually daily, and is subject to demand cycles that regrettably do not coincide with the cow's production cycles. Recognizing that milk is a valuable agricultural product uniquely important to the health and welfare of consumers, the California Legislature adopted the minimum pricing system to ensure an adequate and continuous supply of pure fresh, wholesome milk available at reasonable prices to California's citizens and residents. *See* Cal. Food & Agric. Code §§ 61802, 61805; *Golden Cheese v. Voss*, 230 Cal. App. 3d 547, 553, 281 Cal. Rptr. 587, 589 (1991); *E.M. Consumer Corp. v. Christensen*, 47 Cal. App. 3d 642, 647, 121 Cal. Rptr. 177, 181 (1975).

As in Federal Milk Marketing Orders, the California Stabilization and Marketing Act and Plans classify the minimum prices for raw milk according to the ultimate use to which the processor puts the milk, e.g., fluid milk for consumption as a beverage, heavy creams, sour cream, ice cream, yogurt, cheese, butter, and milk powder.[5] The classifications are stratified essentially according the economic and societal value of the end product. *See* Cal. Food & Agric. Code §§ 61931-61937, 62062, 62079; *see, e.g.*, the N. Cal. Stab. & Mktg. Plan § 300.0. Currently, as in 1997, five classes of prices exist under the California Stabilization and Marketing Act (similar to the multiple classes in Federal Milk Marketing Orders), with Class 1 (primarily fluid milk) as the highest class, and then ranging downward to the lowest classes for products used for supply balancing purposes, Class 4a (butter and powder) and 4b (cheese). *See* Cal. Food & Agric. Code §§ 61932-61935.

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5. California actually applies its classified pricing structure to the components of milk – the butterfat, the solid-not-fats (e.g., protein, calcium, etc.) and, in the case of Class 1, the fluid carrier. Cal. Food & Agric. Code § 62075; *see, e.g.*, the Stabilization and Marketing Plan for Market Milk, as Amended, for the Northern California Marketing Area (the "N. Cal. Stab. & Mktg. Plan") § 300.0, *http://www.cdfa.ca.gov/dairy/stabplan/mcastabplan.pdf*.

B. The Milk Pooling Act and Pool Equalization Funds.

California's implementation of minimum classified pricing by itself was not sufficient to stabilize the California milk production industry. Because dairy farmers most desired the higher Class 1 price, a processor could exact abusive concessions from a dairy farmer in exchange for granting that farmer a Class 1 contract. Abuses by processors ranged from requiring under-the-table rebates, to more sophisticated devices, such as requiring a dairy farmer to lease or buy essentially unproductive land or to pay for in-retail store advertising, or to pay for services such as bulk tank rentals. Class 1 contracts became so desirable that they developed an independent value, and a "contract rights" system developed whereby producers would pay for such rights.

To correct the abuses the minimum classified pricing system fostered, California adopted the original Milk Pooling Act in 1967. The Milk Pooling Plan implemented thereunder further stabilized the California dairy industry by creating a pricing system for the payment of individual farmers that severed the direct connection between the price each dairy farmer received for its milk and the use made of the milk it sold. The Milk Pooling Plan accomplished this by pooling revenues of processor purchases of raw milk, deriving producer prices therefrom, and then requiring California processors to pay individual California dairy farmers one or more pool prices, regardless of the uses to which the milk was put by the processor, rather than the minimum classified prices themselves. The pooling system also created pool equalization funds to which the processors had to account for any difference between the amounts they paid the individual farmers and the minimum classified price of the milk the processors purchased. The system of pricing and pooling was similar, in many respects, to blended pricing and pooling systems adopted by Federal Milk Marketing Orders.

1. Payment to California Farmers.

When implementing the new system of pooling in 1969, California recognized the significant investment many California farmers had made in Class 1 contracts, and, rather

than create a single minimum blend price to pay farmers, as Federal Milk Marketing Orders did, California created a multi-tier pricing system. In 1969, each producer in California was issued an allotment equal to 110% of such producer's historical Class 1 sales, measured in pounds, or "quota." *See* Cal. Food & Agric. Code § 62707. To further equalize returns among producers additional quota was issued to California producers in 1978. *See* Cal. Food & Agric. Code § 62707.1.

For the month of December 2002, only 68, or 3.4% of California's total of 1,984 producers had over 95% (hereinafter, for simplicity referred to as "100% quota holders") of their production covered by quota; 1,517, or 76.5%, had 50% or less of their production covered by quota; and 646, or 32.6%, had no quota at all. Measured in terms of pounds of solids, only 27% of California's December 2002 production was covered by quota. CAL. DEPT. OF FOOD AND AGRIC. ("CDFA"), MILK POOLING BRANCH, REPORT 120-7, 1/24/03, at 41, attached hereto as Appendix B. California producers can buy and sell their quota, and quota has a substantial market value due to the costs incurred to obtain it and the higher price to which quota entitles a farmer, as discussed below.

Since 1994, California processors have paid individual dairy farmers one of two different minimum blended prices for the raw milk they purchased: the higher "quota price" or the lower "overbase price". *See* Milk Pooling Act §§ 62750-62756; Pooling Plan § 906. While the methods for determining the quota price and the overbase price have changed over time, the pricing system operates so that the monthly Class 1 price is always, with a few exceptions, higher than the quota price, which is higher than the overbase price.[6]

A California processor pays a California dairy farmer the quota price for the pounds of milk the farmer sells that is equal to his quota allotment, and the overbase price for those pounds not covered by his quota allotment – regardless of the use to

6. Please see Appendix C, section A, attached hereto, for a description of the two different methods that have been used to determine the quota and overbase prices.

which the processor puts the milk, e.g., fluid milk (Class 1) or cheese (Class 4b). Pooling Plan § 1001.[7]

2. Obligations of California Processors to the Pool.

The Pooling Plan requires a California processor to account to the pool equalization funds for raw milk purchases based on the use to which such raw milk was put and the classified minimum price for such use. *See* Pooling Plan §§ 900, 1003 and 1004. The purpose of the fund is to account for the difference between the direct payments processors make to individual farmers and the minimum classified prices for which the processor is liable.

For example, a processor operating a Class 1 plant, which processes all of the raw milk purchased for use as fluid milk, must account to the pool in an amount determined by multiplying the total pounds of raw milk purchased by the Class 1 price, which, for a Class 1 plant, is effectively the "in-plant blend price." The Class 1 plant will have paid its producers for the raw milk at the overbase price, the quota price, or some combination thereof, depending on the amount of quota, if any, held by the producers. Since the Class 1 price is, with only a few past exceptions, higher than the quota and overbase prices, the Class 1 plant will owe the pool the difference between the Class 1 price and a credit equal to the total amount paid to the producers.

On the other hand, a plant that processes the raw milk it purchases for cheese (Class 4b) must account to the pool in an amount determined by multiplying the total pounds of raw milk purchased by the Class 4b price. Again, the Class 4b plant will have paid its producers at the overbase price, the quota price, or some combination thereof, depending on the amount of quota, if any, held by the producers. If, as is the case with few exceptions, the total amount the Class 4b plant paid to

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7. Accordingly, a farmer that owned quota equal to his entire production volume would receive the quota price on all of the milk he sells; a farmer that owned quota equal to 50% of his entire production volume would receive the quota price on 50% of the milk he sells, and the overbase price on the remaining 50% of milk sold; and a farmer that did not own any quota would receive the overbase price on all milk sold.

producers is greater than the amount for which it must account to the pool, the pool will pay the Class 4b plant the difference.

C. The Challenged 1997 Amendment to the Milk Pooling Plan.

In 1997, the Respondent California Secretary of Agriculture modified the Milk Pooling Plan to address a significant, and unintended, artificial regulatory incentive the previous Milk Pooling Plan created for California processors to purchase milk for Class 1 use from out-of-state producers. Until 1997, a California Class 1 processor that purchased out-of-state milk accounted to the pool at the Class 1 price but could deduct such sales from its pool obligation at the plant's in-plant blend price. Since the in-plant blend price equaled the Class 1 price, this effectively zeroed out the processor's obligation to the pool. Due to the difference in the pool credits a Class 1 processor received for in-state and out-of-state milk, a Class 1 processor would almost always owe the pool the difference between the Class 1 price and the amount paid to California producers, but would never owe the pool money for milk purchased from out-of-state. Accordingly, a California Class 1 processor increased its profits when it paid an out-of-state producer something less than the Class 1 price, even a price, as typically was the case, at least equal to and often above the California quota price.

As a result, prior to the 1997 Amendment, the Pooling Plan treated *every* out-of-state producer better than *any* California producer. Due to the artificial regulatory incentive, out-of-state producers could command prices for Class 1 milk at least equal to, and possibly more than, the California quota price, even though the out-of-state producer had never paid for any quota. At the same time, *no* California farmer could receive more than the quota price, and only that small number (3.4%) of California farmers that held virtually 100% quota could achieve the quota price. The vast majority (96.6%) of California producers would receive something less than the quota price—either a blend of the quota and overbase price, depending on the amount of their quota holdings, or, if they were among the 32.6% of California farmers that held no quota,

the overbase price. Therefore, prior to the 1997 Amendment, the *Pooling Plan itself*—rather than any economic competitive advantage possessed by out-of-state producers—created both the motivation for processors to buy Class 1 milk from out-of-state and the opportunity for out-of-state producers to command higher prices than California farmers. Indeed, from a purely economic standpoint, absent the favorable regulation, out-of-state producers were at a competitive disadvantage because of greater hauling costs.

The unfairness was so great and the advantage offered to "out-of-state" milk so significant that, despite the added *double*-haul costs, some California producers found it to their economic advantage to "round-trip" their raw milk, that is, to ship it out of California and then bring back into California an equivalent amount of milk or sometimes the very same milk. A California "round-tripper" could receive a price somewhere in between the quota price and the Class 1 price for the milk brought back in from out-of-state, whereas if he shipped the same amount of California milk directly to the same processor for the same use, he would receive, at best, the quota price and, much more likely, a blend of the quota and overbase prices, or perhaps just the overbase price. The California Department of Food and Agriculture noted that, by encouraging "round-tripping", the "existing regulatory distortion" in the pre-1997 Pooling Plan "fosters the inefficient movement of milk . . . with significant increases in transportation and labor costs, expanded environmental costs and introduced a speculation factor. . . ." STATEMENT OF DETERMINATION REGARDING THE PROPOSED AMENDMENTS TO THE POOLING PLAN FOR MARKET MILK BASED ON PUBLIC HEARINGS HELD ON DECEMBER 6, 1996, AND FEBRUARY 4, 1997, at 48. The CDFA concluded that, contrary to the dictates of Section 61802(e) of the Food and Agricultural Code, by fostering the wasteful and inefficient practice of "round-tripping", the existing regulation did not "'*promote . . . intelligent marketing* . . . [nor tend] . . . *to eliminate economic waste*' and thus, is not in the public interest." *Id.* at 65.

To reduce the artificial incentive the then-existing Milk Pooling Plan created for Class 1 processors to supply their

needs from out-of-state milk and to eliminate "round-tripping", the 1997 Amendment to the Pooling Plan, provided that, for "other source" milk, which includes out-of-state milk, the processor would receive a credit against its obligation to the pool equal to the lesser of the in-plant blend price or the quota price. Pooling Plan § 900(d). Since the in-plant blend price for Class 1 plants is equal to the Class 1 price, as a practical matter, the credit given to Class 1 plants for out-of-state milk is the quota price.

In actuality, the "quota price" credited to California processors for out-of-state milk purchases is *greater* than the quota price credit processors receive for in-state milk. First, to determine the prices paid to California producers, the total of all transportation allowances paid to California farmers and transportation credits given to California processors is deducted, thus reducing the quota price received by California quota holders.[8] However, an adjustment called the Pool Price Modification Rate adds these amounts back into the "quota price" that California processors receive as a credit for out-of-state milk. Thus, processors receive an enhanced credit for milk purchased from out-of-state, greater than the credit for purchases of in-state milk. Pooling Plan §§ 132, 900(d). In addition, a majority of California producers do not receive the full quota price because they are subject to Regional Quota Adjusters, which are deductions from the quota price established to reflect part of the location value of milk and historical differences of the costs of production within the State. *See* Pooling Plan §§ 910, 910.1, and 914.

Significantly, the 1997 Amendment did not entirely eliminate the artificial incentive for California Class 1 processors to purchase out-of-state milk. Under the 1997 Amendment, because a California Class 1 processor receives a credit for the out-of-state milk somewhat higher than the quota price it pays for in-state milk, that processor has *a somewhat greater* incentive to purchase milk from *any* out-of-state producer as from one of the only 3.4% of California farmers that hold 100% quota. Furthermore, a California Class

8. See Appendix C, section B, for an explanation of transportation allowances and credits.

1 processor has *a substantially greater* incentive to purchase milk from *any* out-of-state producer than from the remaining 96.6% of California dairy farmers, who are entitled to receive a price for their milk somewhere between quota and overbase. These incentives exist because the Class 1 processor profits from the difference between the enhanced quota credit it receives for out-of-state milk and the amount it actually pays to the out-of-state producer. Thus, the 1997 Amendment always positions every out-of-state producer, none of whom has paid for quota, somewhat better than small percentage of California producers who have paid for quota to cover 100% of their production, and far better then the overwhelming majority of California producers.

Actual experience since adopting the 1997 Amendment demonstrates that, indeed, the 1997 Amendment has not imposed a barrier to the importation of out-of-state milk into California for Class 1 uses. On the contrary, the incentive to Class 1 processors to purchase out-of-state milk still exists, as evidenced by a continuing increase of shipment of out-of-state milk to Class 1 processors. In January 2000, out-of-state milk represented only 1.65% of the total production received by processors in California, but 8.48% of all the Class 1 solids-not-fat utilized in California. Since then, importation of out-of-state milk for Class 1 uses has increased steadily so that as of December 2002, it represented 19.2% of California Class 1 solids usage, 226% of what it was in January 2000. *See* CDFA: BULK MILK SHIPPED INTO CALIFORNIA POOL PLANTS FROM OUT-OF STATE SOURCES, Appendix D.

SUMMARY OF ARGUMENT

The merits of Petitioners' Commerce Clause and Privileges and Immunities Clause claims are not before the Court, as both Petitioners and the Solicitor General concede. However since both Petitioners and certain *amici*, including the Solicitor General, nonetheless extensively argue the merits, *Amicus* Western United Dairymen submits that neither claim is valid.

The challenged 1997 California Pooling Plan Amendment is part of a valid exercise of California's police power designed to insure the citizens of California both an adequate supply of

milk and a high quality of milk by means of a complex regulatory system encompassing minimum dairy farmer prices, revenue pooling and standards of composition.

The challenged Amendment neither discriminates against nor burdens interstate commerce. It is designed to address an unintended incentive created by California's Pooling Plan provisions regarding the accounting by California processors to the California pool for purchases for Class 1 (fluid) uses that favors the purchase of out-of-state milk over California milk. That incentive was not the result of any economic or competitive advantage possessed by out-of-state dairy farmers, but rather solely the result of the regulatory quirk that favored out-of-state producers.

The 1997 Amendment merely reduces the artificial regulatory incentive and still treats out-of-state dairy farmers somewhat more favorably that the 3.4% of California producers owning 100% (or almost 100%) quota, and much more favorably than the remaining 96.6% of California producers. The Amendment is neither a subsidy nor a tax. Petitioners have no Constitutional entitlement to the continuation of a California regulatory scheme that is skewed in their favor.

California's pooling and pricing laws and regulations and its compositional requirements are part of a complex regulatory scheme designed to assure both the content and the adequacy of supply of milk to California's consumers. The Ninth Circuit correctly found that California's pooling and pricing regulations and those concerning the content of milk are closely related and that therefore all are within the exemption provided by 7 U.S.C. § 7254.

And, whatever section 7254 exempts—be it California's pooling and pricing laws and regulations, as well as composition and labeling requirements (as urged by Respondents and this *Amicus*) or only composition and labeling (as urged by Petitioners)—the exemption extends to foreclose Commerce Clause scrutiny. Both the language of the statute and the context from which it arose clearly indicate that Congress intended to give California the freedom to adopt its own regulatory standards. Accordingly, the Ninth Circuit

correctly interpreted the term "any other provision of law" to encompass the Commerce Clause of the Constitution. Any other interpretation would render the exemption granted virtually meaningless. However, should this Court interpret the statute as exempting only composition and labeling, there would be no need to reach the Constitutional issue of whether exemption from the Commerce Clause was intended.

The 1997 Amendment does not discriminate, on its face or in practical effect (assuming that is a viable Privileges and Immunities criterion), on the basis of residency or citizenship. In the first place, as indicated in the discussion on the Commerce Clause, it does not discriminate against out-of-state interests at all. Indeed, out-of-state producers are treated more favorably than California producers. Second, the Amendment does not make a distinction on the basis of state residency or citizenship, either on its face or in its practical effect. Out-of-state residents who own dairy farms in California are treated the same as California residents owning dairy farms within the state. And, conversely, California residents owning dairy farms outside the state who sell milk from those farms to California processors for Class 1 uses are treated identically to out-of-state residents who do likewise.

ARGUMENT

I. Whether Or Not California's Milk Pooling Plan, As Amended In 1997, Violates The Dormant Commerce Clause Or The Privileges And Immunities Clause Is Not Before The Court.

The questions before the Court are: (A) whether the exemption granted by 7 U.S.C. § 7254 extends to California's pricing and pooling regulations; and (B) whether an individual can state a claim for a violation of the Privileges and Immunities Clause where a state law distinguishes on its face upon whether a farm is located in-state or out-of-state and not between the "residency" or "citizenship" of the individuals that own or operate the farm.[9] Western United Dairymen

9. Western United Dairymen contends in Section III, *infra*, that 7 U.S.C. § 7254 does, in fact, exempt California's pricing and pooling system from (Cont'd)

concurs with Petitioners that the merits of the Constitutional claims are not before the Court.[10] Indeed, should the Court decide to reverse the decision below on the Questions Presented, Western United Dairymen urges that the Court make no predetermination of the Constitutional questions. Rather, as suggested both by Petitioners and the Solicitor General (*Brief for Petitioners*, hereinafter "*PB*", at 5-6; *Petition for Certiorari Brief for the United States*, filed Dec. 4, 2002, at 10-11, 32-34), if the Court were to reverse the Ninth Circuit, the cases ought to be remanded to the trial courts below for their consideration in the first instance since the Constitutional issues have not yet been fully developed.

Nonetheless, since—despite their concession that the Constitutional questions are not before the Court—both Petitioners (*PB* at 34-49) and various *amici* have stridently argued that the challenged 1997 Amendment to California's Pooling Plan violates both the Commerce and the Privileges and Immunities Clauses, Western United Dairymen feel it is incumbent upon them to demonstrate that the 1997 Amendment is a valid exercise of California's police powers that does not violate either Constitutional provision, even if they were to apply to California's pricing and pooling system.

II. California's Milk Pricing And Pooling System Is A Valid Exercise Of Its Police Powers To Foster Its Dairy Industry.

To foster its domestic dairy industry, California has exercised its right to maintain its own regulatory system governing milk production and pricing. The power of a state to regulate milk pricing is well-established. *See, e.g., Penn Dairies, Inc. v. Milk Control Comm'n of Pa.*, 318 U.S. 261, 278-279 (1943) (upholding the application of Pennsylvania's minimum pricing law to purchases by the federal

(Cont'd)

the Commerce Clause; in Section IV, *infra*, that because the 1997 Amendment does not discriminate against citizens of other states it does not violate the Privileges and Immunities Clause; and, therefore, that the Ninth Circuit's decision should be upheld.

10. Petitioners so concede on pages 4 through 6 of their brief on the merits.

government); *Highland Farms Dairy, Inc. v. Agnew*, 300 U.S. 608, 611 (1937) (citing a line of cases upholding "[t]he power of a state to fix a minimum price for milk"). Furthermore, in the words of this Court, "[n]o one disputes that a State may enact laws pursuant to its police powers that have the purpose and effect of encouraging domestic industry." *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 271 (1984).

To curb destructive trade practices and stabilize its dairy industry, California first exercised its undisputed authority to regulate milk production and pricing in 1935 by enacting the Young Act. California has fostered its dairy industry through regulation ever since, and currently maintains three complex integrated regulatory programs: standards of composition of milk, including fluid milk, under the Milk and Milk Products Act of 1947, and minimum prices to be paid to producers and producer equalization pools under the Stabilization and Marketing Act and the Milk Pooling Act, and their related Plans. The California Legislature adopted the minimum pricing system to ensure an adequate and continuous supply of pure, fresh, wholesome milk available at reasonable prices to California's citizens and residents. Accordingly, the California Supreme Court has repeatedly upheld the minimum pricing system as an appropriate exercise of the State's police powers. *See, e.g., Jersey Maid Milk Prod. Co. v. Brock*, 13 Cal. 2d 620, 636-638, 91 P.2d 577, 587-588 (1939).

As California acted in the 1930's to stabilize its dairy industry through regulation, the Federal government enacted a parallel regulatory system. Responding to similar destructive trade practices, the Federal government, in 1937, implemented the Federal Marketing Act. The Federal government's entry into the field of milk pricing regulation did not pre-empt a state's authority to regulate its own dairy industry (*see Parker v. Brown*, 317 U.S. 341, 354 (1943)); rather, the Federal Marketing Act authorizes the U.S. Secretary of Agriculture to issue regional Federal Milk Marketing Orders at the behest of handlers and/or producers within a marketing area.[11]

11. Notably, Congress has expressly granted California dairy producers the right to elect entry into a separate federal milk marketing order governing the State of California. *See* 7 U.S.C. § 7253(a)(2).

California is one of several areas of the United States that are not governed by Federal Milk Marketing Orders. *See* Appendix A.

Under the *Penn Dairies* and *Highland Farms Dairy* line of cases, *Bacchus*, and the *Jersey Maid* line of cases, *supra*, California clearly has the authority to foster its domestic dairy industry through regulation. Furthermore, as *Parker*, *supra*, makes clear, California's legitimate exercise of its police power to regulate its own dairy industry is not curtailed by the existence of the parallel Federal system, since California's dairy producers have not opted into the Federal system.

Petitioners, and the *amici* supporting them, assail California's milk pricing and pooling system on the grounds that: "California was able, through pooling, to bring about blend prices that were high enough to provide adequate income to dairy farmers to encourage growth in milk production, while also providing . . . an incentive to locate manufacturing facilities in California" (*PB* at 37); the system "is not tempered by the law of supply and demand" (*Brief on the Merits for Amici Curiae Nev., Minn., Mont. Or., Wash., and Wis.* at 2); and that it "encourage[s] its in-state dairy producers to expand production" (*Id.* at 6.); and other similar grounds. These attacks are wholly without legal merit. They amount to nothing more than a claim that the Federal judiciary should restrict California's milk regulation system simply because it is successful and its success has enabled California to become a national player in the dairy industry. California is entitled to continue to exercise its police powers to regulate its dairy industry and to foster its growth, within the bounds of Federal law to which it is subject.

III. The 1997 Amendment of California's Milk Pooling Plan Does Not Violate The Dormant Commerce Clause Or The Privileges And Immunities Clause.

A. The 1997 Amendment Does Not Discriminate Against Interstate Commerce Or Citizens Of Other States.

California's Milk Pooling Plan, as amended in 1997, does not discriminate against interstate commerce or citizens of other states or give California farmers an advantage in the

interstate marketplace. Indeed, even as amended, California's pricing and pooling system places milk that is produced by farms outside of California in a better position than it does milk produced in California, creating greater incentives for the purchase of Class 1 milk from out-of-state and for equal or higher payments to out-of-state farmers.

As set forth in Section II.A above, "[n]o one disputes that a State may enact laws pursuant to its police powers that have the purpose and effect of encouraging domestic industry." *Bacchus, supra*, 468 U.S. at 271. A State is prohibited, however, from "plac[ing] burdens on the flow of commerce across its borders that commerce wholly within those borders would not bear." *Fulton Corp. v. Faulkner*, 516 U.S. 325, 330-331 (1996). Accordingly, a State may not discriminate against interstate commerce, i.e., impose "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." *Oregon Waste Sys. Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 99 (1994). A State, however, may impose a "compensatory tax" on interstate commerce if it is "designed simply to make interstate commerce bear a burden already borne by intrastate commerce." *Associated Indus. of Mo. v. Lohme*, 511 U.S. 641, 647 (1994).

1. The 1997 Amendment Reduces An Artificial Regulatory Incentive Favoring The Purchase Of Out-Of-State Milk Over In-State Milk.

As set forth in detail on pages 7 through 8, *supra*, prior to 1997, the Milk Pooling Plan treated out-of-state milk more favorably than in-state milk for purposes of a California processor's obligations to the pool. This more favorable treatment permitted California processors to pay more to all out-of-state producers than to the best paid California producers, but end up paying less for the milk. It, thus, created a strong incentive to purchase milk for Class 1 use from out-of-state and placed *every* out-of-state producer in a better position than *any* California producer, to the point of encouraging the wasteful and destructive practice of "round tripping" by California producers.

California's pricing and pooling system, which was intended to stabilize the industry and to promote public health and welfare, thus harbored a perverse unintended incentive that could be, and was, manipulated to destabilize the industry and to engage in marketing practices that contravened the public interest. In response, the Respondent California Secretary of Agriculture implemented the 1997 Amendment.

California is not alone in its need to close this regulatory loophole to achieve "competitive parity" between pool (in-state) and non-pool (out-of-state) milk. The parallel Federal pricing and pooling system faces the same problem – the need to "neutralize, compensate for and eliminate the artificial economic advantage for non-pool milk which necessarily is created by the classified pricing and pooling of pool milk under the order." *Lehigh, supra*, 370 U.S. at 84. Furthermore, just as States are prohibited by the dormant Commerce Clause from imposing discriminatory burdens on interstate commerce, the U.S. Secretary of Agriculture is prohibited by statute from imposing "trade barriers" on entry of commerce into a Federal Milk Marketing Area.[12]

In *Lehigh*, the U.S. Secretary of Agriculture attempted to achieve competitive parity between pool milk under the New York-New Jersey Milk Marketing Order and non-pool (i.e., out-of-area) milk by requiring a handler of non-pool milk to make a "compensatory payment" to the pool. Farmers in the New York-New Jersey Marketing area received a uniform minimum blend price, rather than the minimum classified prices. Nonetheless, the U.S. Secretary of Agriculture, imposed on processors that purchased non-pool milk a "compensatory payment" in an amount equal to the difference between the minimum prices for the highest and for the lowest use classifications, i.e., Class I and Class III prices, under the New York-New Jersey Milk Marketing Order. *Lehigh, supra*, 370 U.S. at 83.

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12. Section 608(c)(5)(G) of the Federal Marketing Act provides: "No marketing agreement or order applicable to milk and its products in any marketing area shall prohibit or in any manner limit, in the case of products of milk, the marketing in that area of any milk or product thereof produced in any production area in the United States."

This Court struck down the Secretary's regulation as erecting an impermissible "trade barrier" because it would "in all but rare instances, nullify any competitive advantage that non-pool milk could have" since a handler would have an incentive to bring non-pool milk in the area only where its cost was less than the minimum price for the lowest use, Class III. *Id.* at 84. In striking down, the compensatory payment in *Lehigh*, however, this Court suggested that to achieve competitive parity between pool milk and non-pool milk a payment equal to the difference between the Class I price and the blend price would be acceptable. *Id.* at 86-87 n.13.

Petitioners wrongly cite the *Lehigh* decision to support their challenge, disingenuously stating that the 1997 Amendment "closely resembles the credit and compensatory payment . . . condemned as a trade barrier in *Lehigh*." *PB* at 40. To the contrary, the 1997 Amendment's adjustment of the credit that California Class 1 processors receive for their purchase of out-of-state raw milk is quite unlike the impermissibly discriminatory payment required by the U.S. Secretary of Agriculture in *Lehigh*. Due to the draconian payment required in *Lehigh*, *no* non-pool farmer would be able to enter the market of the Marketing Area unless it could afford to sell its milk for the Class III price or less. At the same time, *all* of the pool farmers were entitled to obtain the higher uniform blend price. In other words, the impermissible compensatory payment imposed in *Lehigh* had the effect of placing *every* non-pool producer in a worse position than *all* of the pool producers—in stark contrast to the 1997 Amendment, which still places *every* out-of-state producer in a *better* position than *any* in-state producer. Indeed, to be comparable to the compensatory payment struck down in *Lehigh*, the 1997 Amendment would have had to credit the processor with payment of only the 4a or 4b price (the lowest minimum classified prices in California) and require the processor to pay the difference between the Class 1 price and the Class 4a or 4b price to the pool.

The 1997 amendment is, in fact, more comparable to the method of achieving "competitive parity" that this Court, in *Lehigh*, suggested was acceptable and which the Seventh

Circuit upheld in *County Line Cheese Co. v. Lyng*, 823 F.2d 1127 (1987)—having the Class 1 processor account to the pool for the difference between the Class 1 price and the uniform blend price actually paid to the pool producers. The Seventh Circuit in *County Line Cheese* determined that the payments for non-pool milk required under the Indiana Federal Milk Marketing Order "do not present a trade barrier", but simply "erase an artificial advantage gained by the way the price supports work." *County Line Cheese, supra*, 823 F.2d at 1134. In upholding the Indiana Federal Milk Marketing Order, the Seventh Circuit reasoned that "[n]or do the regulations at issue here prescribe minimum prices that handlers pay for nonpool milk; if anything, they act to lower the maximum amount that handlers will be willing to pay for nonpool milk." *Id.* at 1135.

Notably, the 1997 Amendment is more even-handed than the method for achieving competitive parity approved in *County Line Cheese*. First, the 1997 Amendment has set the credit for out-of-state milk at the *highest* price that only a handful (3.4%) of California producers receive. Furthermore, in actuality, as Petitioners concede, the credit a processor receives for the purchase of out-of-state milk "is actually a modified quota price . . . approximately 3 cents higher than the quota price." *PB* at 40 n.5. Thus, rather than presenting a trade barrier, the 1997 Amendment actually treats every out-of-state producer *somewhat better than* the best positioned California producers, the handful that have paid for quota to cover 100% of their production.

Furthermore, actual experience after the 1997 Amendment demonstrates that, indeed, the 1997 Amendment did not impose a barrier to the importation of out-of-state milk into California for Class 1 uses. The continuing incentive to Class 1 processors to purchase out-of-state milk, in fact, has fueled an increase in shipments of out-of-state milk to Class 1 processors, with such shipments increasing by 116% in just the past three years.

2. The 1997 Amendment Does Not Benefit California Farmers Through A Direct Subsidy Funded By Out-Of-State Milk.

Petitioners wrongly claim that the 1997 Amendment "violated" *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, (1994) by "subject[ing] out-of-state dairy farms to disparate treatment that benefited California farmers at the expense of out-of-state farmers." *PB* at 41. In *West Lynn Creamery*, Massachusetts fluid milk dealers challenged a Massachusetts pricing order that required them to pay a tax on all fluid milk they sold to Massachusetts retailers – regardless of the origin of the milk even though out-of-state milk accounted for two-thirds of the milk sold. This uniform tax was imposed on top of the minimum price set by the Federal Milk Marketing Order governing the Massachusetts farmers. The tax was then distributed to Massachusetts dairy farmers, each Massachusetts producer receiving "a share of the total fund equal to his proportionate contribution to the State's total production of raw milk." *Id.* at 191. The tax was implemented to directly subsidize Massachusetts farmers, who were not able to turn a profit at the minimum price set by the Federal Marketing Order governing them. *Id.* at 191 n. p.5. The pricing order "allow[ed] Massachusetts dairy farmers who produce at a higher cost to sell at or below the price charged by lower cost out-of-state producers." *Id.* at 194-195. The Court in *West Lynn Creamery* struck down this otherwise non-discriminatory tax because, when coupled with the subsidy of in-state farmers, it created a discriminatory burden on out-of-state milk:

> [T]he tax on in-state milk, unlike that imposed on out-of-state milk does not impose any burden on in-state producers, because in-state dairy farmers can be confident that the taxes paid on their milk will be returned to them via the Dairy Equalization Fund. *Id.* at 199 n.16.

West Lynn Creamery presents an entirely different set of facts than the case at bar and is simply inapplicable. By implementing the 1997 Amendment, California is not imposing a tax on the sale of milk by processors to retailers

that is then distributed directly to domestic farmers in an attempt to enable farmers to price their milk as low as the milk of their out-of-state competitors. To the contrary, Petitioners complaint is that out-of-state farmers are no longer able to command as *high* a price for their milk as previously under California's pricing and pooling system, not that California has eliminated their ability to undersell California farmers.[13] The 1997 Amendment is neither a tax nor a subsidy. It simply reduces the regulatory incentive favoring the purchase of Class 1 milk from out-of-state farmers at a higher price than in-state farmers are paid by equalizing the pool credits that Class 1 processors receive for the purchase of out-of-state and in-state milk. There is no tax on anyone and no subsidy to California farmers, who are paid directly by the processors and do not receive any payments from the pool. And to the extent that the operation of the Amendment enhances the quota price, out-of-state producers benefit equally as they are enabled to receive the higher quota price.

B. California Has Not Imposed An Impermissible Minimum Pricing Requirement On The Purchase Of Out-Of-State Milk.

As discussed above, Petitioners' fundamental complaint is not that California has placed a floor under the ability of out-of-state producers to undersell California producers, but that the 1997 Amendment has placed a *ceiling* on the amount by which the price the out-of-state producers receive can *exceed* the price paid to individual California farmers. Like the requirement in *County Line Cheese* that processors account to the pool for out-of-state milk, the 1997 Amendment does not "prescribe minimum prices that handlers pay for nonpool milk"; rather it acts to "lower the maximum amount that handlers will be willing to pay for nonpool milk." *County Line Cheese, supra,* 823 F.2d at 1135. Accordingly, Petitioners' reliance on *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935) is misplaced.

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13. Indeed, Petitioners are explicit about the true nature of their claim, objecting that "under the 1997 amendments, . . . no longer may the out-of-state dairy farmer receive payment of the full value of his transaction – the plant blend price" (i.e., the Class 1 price). *PB* at 39.

In *Baldwin*, the Vermont producers challenged the imposition of New York's minimum price requirements on the Vermont producers because it prevented them from using an *actual economic edge* – their ability to produce milk more cheaply than New York farmers – to undersell New York farmers. Consistent with *Baldwin*, California's Pooling Plan, even as amended in 1997, does not impose a minimum pricing requirement on any interstate transaction. Even after 1997, out-of-state dairy farmers are free to undersell California dairy farmers. Nothing in *Baldwin* requires that a State maintain a regulatory incentive that favors the purchase of out-of-state milk at the same time that it maximizes the price an out-of-state farmer can command.

Significantly, cases such as *Baldwin* and *West Lynn Creamery* deal with regulations that erect barriers to importation of out-of-state or out-of-area milk by producers who have an economic competitive advantage due to cheaper production costs. The 1997 Amendment simply does not impose such a barrier. Out-of-state producers are free to undersell California milk if they have a true economic competitive advantage, as opposed to a regulatory advantage. Petitioners' claim is at its core that they have a Constitutional entitlement to a California regulatory system that guarantees them an opportunity to achieve or approximate the *highest* price under California's minimum classified pricing system, the Class 1 price, a benefit no California producer receives.[14]

C. California Is Not Required To Extend To The Interstate Sale Of Milk The Same Economic Advantages It Gives Its Domestic Industry.

Under the dormant Commerce Clause, California may provide benefits to domestic industry that it does not provide to out-of-state interests. "The Commerce Clause does not

14. Petitioners have provided in an Appendix a June 19, 1997, opinion of the Legislative Counsel of California. That opinion is off the mark as it is based on the totally erroneous premise, that, under the Amendment, out-of-state producers could receive no more or less than the price paid in-state producers. CAL. LEGIS. COUNSEL OPINION, MILK POOLING #12484, JUNE 19, 1997, at 1a, 6a of Petitioner's Appendix. Nothing in the 1997 Amendment prohibits an out-of-state producer from undercutting the prices paid to California dairy farmers.

prohibit all state action designed to give its residents an advantage in the marketplace, but only action of that description in connection with the State's regulation of interstate commerce." *New Energy Co. of Ind. v. Limbach*, 486 U.S. 269, 278 (1988). For example, "(d)irect subsidization of domestic industry does not ordinarily run afoul of that prohibition." (*Id.*)

Petitioners complain that farms located out-of-state are discriminated against because California does not guarantee them the benefits of "quota". Petitioners lament, "[T]he out-of-state farmer can never receive the true 'benefit' of quota, which includes the assurance of receiving the blend price without regard to competition or plant destination." *PB* at 41. In characterizing the "assurance of receiving" the quota price as a "*benefit*", Petitioners turn *Baldwin, supra*, on its head, as it *struck down* the imposition of minimum pricing requirements on interstate commerce as an impermissible *burden*. Petitioners further object that out-of-state farmers are denied the benefit of quota's "asset value", seeming to claim free entitlement to an asset for which California farmers have paid a substantial price,[15] as Petitioners acknowledge when they state that quota is sold on the market for at least $500 per pound of solids. *Id.* Last, Petitioners complain that out-of-state producers cannot receive the transportation allowance that a small number of California's producers receive, the cost of which all California's dairy farmers pay through a deduction from the prices they receive. Their claim to the transportation allowance is most ironic since Petitioners have conceded that the credit processors receive for out-of-state milk has been adjusted "so that out-of-state milk is not required to fund the transportation allowance program." *PB* at 40.

In addition to disregarding entirely a State's right, under *Bacchus* and *Limbach, supra*, to implement policies and supports directed at its own industry, Petitioners assert an entitlement

15. The 1969 grant of quota in the original Pooling Plan was in recognition of the consideration producers historically paid for Class 1 contracts, either directly by payment for "contract rights" or indirectly through various actual or disguised rebates. *See* p. 4, *ante*. Furthermore, after issuance of additional quota in 1978, most California producers have sold and bought quota as cash investments.

to benefits for which they have never paid and transmute what is otherwise considered an unconstitutional burden into a Constitutional right.

In short, under California's pricing and pooling plan before 1997, *every* out-of-state farmer was better positioned than *any* of California's farmers because an out-of-state farmer could obtain a higher price for Class 1 milk, at less cost to the processor, than any California farmer could obtain. The 1997 Amendment creates a more even playing field by reducing, but not eliminating, the purely regulatory advantage that California's pricing and pooling system gave out-of-state farmers—by treating them as well as, even somewhat better than, California's best paid producers, and far better than the vast majority of its producers. Petitioners' challenge to the 1997 Amendment seeks to turn the Commerce Clause and the Privileges and Immunities Clause on their heads because they invoke these Constitutional provisions not to protect themselves from a discriminatory burden placed on interstate commerce but to demand that California continue to extend them far better treatment than it does any of its own farmers.

IV. 7 U.S.C. § 7254 Exempts California's Milk Pricing And Pooling Regulations From The Dormant Commerce Clause.

A. The Court Should Uphold The Decision Of The Ninth Circuit In The Case At Bar And In *Shamrock*.

1. Section 7254 Applies To California's Pricing And Pooling Regulations.

Western United Dairymen concur with the Respondent California Secretary of Agriculture's position, as set forth in its brief on the merits, that the exemption from all provisions of Federal law granted pursuant to 7 U.S.C. § 7254 applies to California's pricing and pooling regulations. As discussed previously, California uses a system of three interrelated programs to regulate milk: standards of composition under the Milk and Milk Products Act; classified minimum producer pricing under the Stabilization and Marketing Act; and milk pooling under the Milk Pooling Act. Indeed, the first of these statutes to be enacted, the Stabilization and Marketing Act,

expressly recognized the integrated relationship between pricing and composition of milk. In defining the purpose of the Marketing Act, the California Legislature declared that:

* * *

> (b) The production and maintenance of an adequate supply of healthful market milk of *proper chemical and physical content*, free from contamination, is vital to the public health and welfare . . .
>
> (c) [T]he potential exists for economic disruption . . . in the production, marketing, and sale of market milk which may constitute a menace to the health and welfare of the inhabitants of this state and may tend to undermine . . . *standards of content* and purity. . . .

Cal. Food & Agric. Code § 61802 (emphasis added).

2. The Section 7254 Exemption Encompasses The Commerce Clause.

Both the Petitioners and the Solicitor General argue that Section 7254 does not exempt the subject matter it governs from the Commerce Clause. *PB* at 4, 23-25; *Brief on the Merits for the United States ("U.S. Brief")* at 10-14. Each relies heavily on the use in Section 7254 of the words "shall be construed" as an indication that Congress did not intend the phrase "this Act or any other provision of law" to include only statutory law and not the Commerce Clause.

Use of the verb "construe" indicates no such thing, however. The common and preferred meanings of "construe" are: "1. to give the meaning or intention of; explain; interpret; 2. to deduce by inference or interpretation; to infer. . . ." RANDOM HOUSE WEBSTER'S UNABRIDGED DICTIONARY (2d ed. 1999). As the Commerce Clause is an affirmative grant of power to Congress to regulate interstate commerce, the proscriptions against interference by states are perforce deduced or inferred from the affirmative grant. Indeed, the Solicitor General concludes that "[t]he Commerce Clause, in contrast, is a structural provision of the Constitution, which is expressly

addressed to the powers of Congress, and which only by implication contains the powers of states." *U.S. Brief* at 26. Thus every dormant Commerce Clause case requires courts to "construe" the Commerce Clause as applied to the facts of the case. Accordingly, the word "construe" does not indicate that Congress intended to exclude the Commerce Clause from the meaning of "any other provision of law" used in Section 7254. Indeed, the more reasonable view is that Congress intended to include the Commerce Clause in its exemption.

Petitioner's assertion that the pairing of the words "this Act" and "any other provision of law" is a "powerful indication" that Congress "had statutory law in mind" is simply *ex cathedra* without support in precedent or logic. At worst, that "pairing" is equally consistent with a Congressional intent to exempt the Commerce Clause as well as statutory law.

The context from which Section 7254 arose strongly suggests that exemption from the Commerce Clause was intended. If one accepts Petitioner's assertion that Congress intended Section 7254 to exempt only California's compositional standards and labeling regulations, the Congressional intent to include the Commerce Clause within the body of law from which these regulations are exempt becomes even clearer. Under provisions of the Nutrition Labeling and Education Act of 1990 ("NLEA"), 21 U.S.C. § 343-1, states were prohibited from adopting standards of identity (i.e., compositional standards) different from federal standards. Other than the NLEA, the only other applicable restriction over which Congress had the power to exempt was the Commerce Clause. Congress' undeniable intent was to allow California to have its own standards of composition of milk and labeling requirements. To permit that, Congress had to exempt California's regulations from two bodies of law, the NLEA and the Commerce Clause.

If Congress had intended the exemption to cover only the provisions of NLEA, it could have so provided. From its use of the term "*any* other provision of law," it is most reasonable to construe Congress' intent to have included the other "provisions of law" that might be applicable - the NLEA and

the Commerce Clause.[16] Since the purpose of the exemption was to allow California regulatory freedom with respect to a product distributed extensively in interstate commerce, failure of the exemption to include the Commerce Clause would render that intent meaningless. True, the statute does not expressly refer to the Commerce Clause or the Constitution, but as the Solicitor General has noted, Congress has not always made specific reference to the Constitution when its intent extended to the Constitution and other sources of law.[17] *U.S. Brief* at 12.

Finally, the Solicitor General suggests that if "any other provision of law" were read to include the Constitution, the exemption would presumably include such Constitutional provisions as the Privileges and Immunities Clause of Article IV and the Equal Protection Clause of the Fourteenth Amendment. Statutes, however, must be interpreted rationally so as to avoid absurdity. Clearly Congress understood that its power to exempt California from the restrictions of Federal law extended to the Commerce Clause but not to Privileges and Immunities or Equal Protection. A Congressional exemption provision must be read to relate only to that which Congress has the power to exempt.

16. Subdivision (b) of 21 U.S.C. § 343-1 provided a means for a state to obtain an exemption from the statute's proscriptions, if, among other things, the U.S. Secretary of Agriculture determined that the state's regulation would not unduly burden interstate commerce. Congress thus clearly had in mind the Commerce Clause when it enacted 21 U.S.C. § 343-1, and in enacting section 7254 must have intended the exemption therein to cover the Commerce Clause.

17. The Solicitor General has referred to a number of federal statutes that refer to the Constitution and "laws" as examples where there was specific reference to the Constitution. *U.S. Brief* at 12 n.3. Interestingly, each statute speaks of the Constitution and "laws," the latter always in the plural. Section 7254 refers to "any other provision of law." This suggests a reference to a larger universe, the body of "law" that might apply to the matters exempted. The Solicitor General also notes the language of Article VI of the Constitution which refers to "[t]his Constitution and the Laws of the United States . . ." presumably to illustrate a distinction made between the Constitution and statutory law. But Article VI goes on to state that together, the Constitution, the Laws of the United States and treaties, "shall be the supreme Law of the Land," thus encompassing the Constitution, statutes and treaties within the meaning of "Law."

B. If The Court Determines That Section 7254 Does Not Apply To The Pooling And Pricing Regulations, The Commerce Clause Issue Need Not Be Decided.

"A fundamental and long-standing principle of judicial restraint requires that courts avoid reaching constitutional questions in advance of the necessity of deciding them." *Lyng v. N.W. Indian Cemetery Prot. Assoc.*, 485 U.S. 439, 445 (1988). Accordingly, the Court has stated that its "established practice is to resolve statutory questions at the outset where to do so might obviate the need to consider a constitutional issue." *United States v. Wells Fargo Bank*, 485 U.S. 351, 354 (1988). Therefore, if the Court should determine that the exemption granted by Section 7254 does not extend to California's pricing and pooling regulations in general, or, in particular, the 1997 Amendment, the Court does not need to determine whether the subject matters undeniably exempted from Federal statutory provisions—compositional standards and labeling—are also exempt from the Commerce Clause. That question, which touches on the Constitution, need not be reached.

V. Because The 1997 Amendment Does Not Discriminate Against Citizens Of Other States, The Ninth Circuit's Decision Below Should Be Upheld.

Petitioners' claim under the Privileges and Immunities Clause is without merit. The threshold for stating a claim for violation of the Privileges and Immunities Clause is that the challenged regulation is in fact discriminatory. If that threshold is not crossed, a viable claim for violation of the Privileges and Immunities Clause does not exist. As established in Section II.B, supra, the 1997 Amendment does not discriminate against out-of-state milk. Indeed, it continues to provide an incentive that favors the purchase of out-of-state milk by California processors.

Additionally, California's pricing and pooling system does not regulate on the basis of an individual's state of citizenship—either on its face or in practice. As the Solicitor General eloquently states in its brief:

> It is far from clear that . . . a motivating purpose of the California regulations was to place the State's own citizens at an advantage over citizens of other

> State. Nothing in those regulations or any other provision of California law prohibits citizens of other States from owning dairy farms in California, And, when citizens of other States *do* own dairy farms in California, the milk produced at those dairy farms is treated identically to milk produced at California dairy farms owned by California citizens . . . By the same token, all raw milk at dairy farms outside California is treated identically, whether the dairy farm is owned by citizens of California or citizens of other States. Indeed, the Petitioners in this case include a California corporation and two California partnerships (with some or all California partners), which complain about the impact of the California regulations on raw milk produced at the dairy farms that they operate in Nevada.

U.S. Brief at 27-28 n. 8 (citations omitted).

To support their right to press a Privileges and Immunities claim despite the apparent lack of connection between California's pricing and pooling regulations and state citizenship, Petitioners rely on *Chalker v. Birmingham & N.W. Ry.*, 249 U.S. 522 (1919). However, *Chalker* is inapposite here. In *Chalker*, an Alabama resident with his principal office in Alabama challenged a Tennessee law that imposed a higher tax on out-of-state construction companies that did business in Tennessee but had their principal office in another state than on Tennessee construction companies or out-of-state construction companies with their principal place of business in Tennessee. In *Chalker*, the Court struck down the higher tax as impermissibly discriminatory, even though it did not discriminate on the basis of citizenship on its face. The *Chalker* court reasoned that: "We can find no adequate basis for taxing individuals according to the location of their chief offices—the classification, we think, is arbitrary and unreasonable." *Chalker, supra*, 249 U.S. at 527.

Unlike in *Chalker*, an easily discernible and legitimate reason exists for State regulation to distinguish between goods based upon where they are produced, i.e., in-state or out-of-state as States ordinarily must comply with the requirements

of Federal law, including the Commerce Clause.[18] Thus, while *Chalker*'s reasoning may be applicable in the tax context, it is entirely inapplicable in the context of commercial regulation. Accordingly, the Solicitor General is correct when he states that: "It does not follow from *Chalker* that every state law that might have a disparate impact on individuals who are not citizens or residents of the State implicates the Privileges and Immunities Clause, as petitioners at times appear to suggest." *U.S. Brief* at 27.

Because the *Chalker* rationale is not applicable in every context, the Solicitor General's concern that broad application of *Chalker* "would raise serious questions about, and perhaps invalidate, a whole range of *** statutes", (*Id.* at 26 (orig. ellipses), *quoting Washington v. Davis*, 426 U.S. 229, 248), is well-taken. Furthermore, with concerns about the impact of a sweeping application of the *Chalker* rationale in mind, the Solicitor General astutely points out that "intervening developments in the Court's approach to evaluating state laws challenged as discriminatory under the Equal Protection Clause", i.e., the requirement that a law have both a discriminatory purpose and effect to be unconstitutional, may be useful for informing the Court's decision on this issue. *Id.* at 28-29.

CONCLUSION

The decision of the Ninth Circuit should be affirmed as it correctly determined that the challenged 1997 Amendment to the California Pooling Plan was exempted under the provisions of 7 U.S.C. § 7254. Petitioners' arguments concerning the Commerce Clause and the Privileges and Immunities Clause, though not before this Court, are without merit. Should the Court determine contrary to the Ninth Circuit decision that, as a matter of statutory interpretation, section 7254 does not exempt California's minimum producer pricing and pooling laws and regulations in general, or the challenged Amendment in particular, the Court need not and should not make any determination as to whether Congress intended the exemption that was granted extends to challenges under the Commerce Clause.

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18. Notably, the distinction in California's Pooling Plan between "other source" milk, which includes out-of-state milk, predates Section 7254's exemption of the Plan from the strictures of the Commerce Clause.

Respectfully submitted,

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APPENDIX A – FEDERAL MILK MARKETING ORDER AREAS, JANUARY 1, 2000

FEDERAL MILK MARKETING ORDER AREAS
January 1, 2000

USDA
Agricultural Marketing Service
Dairy Programs

DIFFERENCES IN SHADING MERELY SERVE TO DIFFERENTIATE BETWEEN MARKETING AREAS

APPENDIX B – CALIFORNIA DEPARTMENT OF FOOD AND AGRICULTURE, MILK POOLING BRANCH, AMOUNT OF QUOTA IN SHIPMENT FOR THE MONTH OF DECEMBER, 2002

PERCENT OF QUOTA IN SHIPMENT
FOR THE MONTH OF DEC, 2002

STATEWIDE

PRODUCTION/QUOTA PERCENT	SOLIDS PRODUCTION	QUOTA SOLIDS	NO OF PRODUCERS	NO AT EQUALIZATION
101 +	1,462,869	2,023,046	40	33
96 - 100	2,825,244	2,771,043	28	22
91 - 95	1,470,161	1,382,155	19	18
86 - 90	4,100,924	3,624,171	34	29
81 - 85	4,385,692	3,676,863	36	31
76 - 80	4,137,800	3,255,709	36	34
71 - 75	7,795,852	5,713,900	50	47
66 - 70	5,700,992	3,896,428	42	38
61 - 65	6,509,757	4,150,399	63	54
56 - 60	7,410,869	4,335,863	56	52
51 - 55	7,602,937	4,071,064	63	56
46 - 50	10,016,952	4,819,656	61	56
41 - 45	10,732,356	4,635,666	69	59
36 - 40	9,938,189	3,796,363	65	61
31 - 35	10,934,885	3,681,998	83	76
26 - 30	12,819,146	3,634,578	90	69
21 - 25	11,486,082	2,727,704	74	52
16 - 20	10,921,757	2,033,831	91	61
11 - 15	11,878,867	1,524,340	101	45
6 - 10	18,109,014	1,588,559	126	41
1 - 5	19,253,260	661,453	111	19
0 -	72,143,689	2,025	646	7
TOTALS:	251,637,294	68,006,814	1,984	960

APPENDIX C – OPERATION OF CALIFORNIA POOLING PLAN

A. Prices Paid To California Farmers.

1. Prior to 1994

The quota allotments granted to California farmers were measured in pounds of the components of milk.[1] Producers were also granted a separate allotment called "production base" equivalent to their historical total production during the selected historical base period. In 1978, additional quota was issued to assist in equalizing returns between producers. Cal. Food & Agric. Code § 62707.1. The Pooling Act and the Pooling Plan also established three revenue equalization pools–a quota pool, a base pool and an overbase pool. Revenues from the sales of raw milk by producers at the various classified prices each month were allocated to each pool: first to the quota pool, then to the base pool and finally to the overbase pool. The revenues were assigned by class, that is, the revenues from Class 1 sales first, Class 2 sales, second, and so on.

The operation of pooling prior to 1994 can best be understood by visualizing the "pools" originally created by the Pooling Act and the Pooling Plan as three side by side containers. The first would be the quota pool. Its size or capacity would be equal to the total number of quota pounds held by all producers. In a given month, all of the revenues from Class 1 sales for the month would be poured into that container. If the number of pounds of such sales did not fill the quota pool container, as was always the case, the revenues for sales of the next lower class or classes in descending order would be poured into the quota pool container until the number of pounds in that pool filled the container's capacity. Then the revenues from the pounds sold of the remaining class or classes, again in descending

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1. As California prices milk on the components thereof, quota was separately allotted for the fat and solids-not fats components.

order, would be poured over into the "base pool" [2] container until the number of pounds in that pool equaled its capacity, measured in pounds. Revenues for the pounds of sales not poured into the quota and base pools went into the overbase pool. Pooling Act §§ 62703, 62707; Pooling Plan §§ 108, 108.5, 200. Then a price for each pool was calculated by dividing the total revenues in that pool by the total pounds in that pool. Pooling Plan §§ 902-904. Since the size of the quota pool in pounds exceeded the number of pounds of Class 1 sales, the revenues of that pool historically included revenues of one or more lower classes, and hence the quota price was really a blend price of revenues from the sales of multiple classes. Generally, except for a few aberrations when market conditions drove the lower class prices higher than the fixed Class 1 price, the Class 1 price exceeded the quota price, and the quota price exceeded the base and overbase prices.

2. Since 1994

In 1993, the California Legislature added sections 62750-62756 to the Pooling Act. Under the new provisions (which became operative commencing 1994) the revenues of sales in all classes, including Class 1, are pooled, separately by the fat and solids-not-fat components, to derive blend overbase prices for each component. As a result, there is established a fats overbase price and a solids overbase price. Then a fixed differential of $1.70 per hundredweight (or $.195 per pound) is added to solids-not-fat overbase price to establish a quota price for solids. Under the 1993 changes, no quota premium is provided for the butterfat component of milk. With a few monthly exceptions, the Class 1 price has exceeded the quota price.[3] The solids quota

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2. The base pool was generally quite small and had a rather insignificant effect on the operation of the pool.

3. In those few instances where the quota price exceeds the Class 1 price, the 1997 Amendment provides the Class 1 plant the same (Cont'd)

price, because of the fixed differential, always exceeds the solids overbase. Pooling Act § 62750; Pooling Plan § 906.

B. Transportation Allowances and Credits.

The prices paid to California farmers are also adjusted by a transportation allowance paid to certain producers and a transportation credit paid to certain processors. Under the Pooling Plan, a few California producers in areas designated as a "supply" areas receive an allowance called the "Transportation Allowance" for shipping milk into areas designated as deficit areas. Pooling Plan §§ 920-923. To encourage shipment by these producers to a more distant Class 1 plant in metropolitan areas rather than to a closer plant the producers receive an allowance to cover the higher transportation costs in order. Only a few California producers receive this allowance, but all California producers pay for it through a deduction of the total cost of these allowances from monthly solids-not-fat revenues before calculating the quota and overbase prices California producers are to receive. Pooling Plan, §§ 906(e)(2)(3), (f) and (g). Likewise, the Stabilization & Marketing Plans provide for transportation credits to plants for interplant shipments of milk. Stabilization & Marketing Plans for both Northern and Southern California § 300.2. Under the Pooling Plan, these credits reduce handlers' pool obligations and are deducted from pool revenues before calculation of the prices to be received by California producers. Pooling Plan §§ 810-814, 906(c)(1), (e)(1). Hence, all California producers pay for the amount of these transportation

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(Cont'd)

credit as prior to the Amendment. Prior to the Amendment, the processor accounted to the pool at Class 1 prices for purchases from out-of-state producers but received a reduction in an equal amount, zeroing its pool obligation. Under Pool Plan section 900(d), added in 1997, a Class 1 plant likewise accounts to the pool for such purchases, but receives a credit for the lower of the in-plant blend price or the quota price. In these few instance, the lower price is the in-plant blend price (which for a Class 1 plant *equals* the Class 1 price), so the processor gets a credit based on that price, again zeroing its obligation to the pool.

credits. However, to determine the credit California processors are to receive for milk purchased from out-of-state sources, the 1997 Amendment enhances the quota price credit by adding these transportation allowances and credits back to the quota price through an additional adjustment called the Pool Price Modification Rate. Pooling Plan, §§ 132, 900(d). Thus, while out-of-state producers have paid nothing for transportation allowances and credits, the pool credit their milk receives, and thus the price they can command, is enhanced by them. The Pool Price Modification Rate exemplifies the painstaking effort taken in the 1997 Amendment to be fair to out-of-state producers.

APPENDIX D – BULK MILK SHIPPED INTO CALIFORNIA POOL PLANTS FROM OUT-OF-STATE SOURCES

Bulk Milk Shipped into California Pool Plants from Out-of-State Sources

Pounds of Milk

Date	Out-of-State (OOS) Milk	CA Milk Production	OOS as % of Total CA Production	Total Solids Production	Total Class 1 Solids	Class 1 % of Total Solids	Total OOS Solids	OOS as % of Total Solids*	OOS as % of Class 1 Solids
Jan-00	44,719,421	2,705,859,000	1.65%	332,838,000	65,098,000	19.56%	*5,518,377*	*1.66%*	*8.48%*
Feb-00	43,404,020	2,555,830,000	1.70%	313,970,000	61,359,000	19.54%	*5,356,056*	*1.71%*	*8.73%*
Mar-00	55,333,211	2,736,425,000	2.02%	335,867,000	66,469,000	19.79%	*6,828,118*	*2.03%*	*10.27%*
Apr-00	49,641,750	2,728,888,000	1.82%	330,926,000	60,123,000	18.17%	*6,125,792*	*1.85%*	*10.19%*
May-00	50,151,090	2,796,218,000	1.79%	337,168,000	64,809,000	19.22%	*6,188,645*	*1.84%*	*9.55%*
Jun-00	48,433,603	2,669,316,000	1.81%	319,327,000	61,463,000	19.25%	*5,976,707*	*1.87%*	*9.72%*
Jul-00	50,800,945	2,781,447,000	1.83%	333,141,000	62,003,000	18.61%	6,160,387	1.85%	9.94%
Aug-00	45,048,766	2,678,687,000	1.68%	322,036,000	64,957,000	20.17%	5,496,778	1.71%	8.46%
Sep-00	43,390,939	2,592,832,000	1.67%	314,563,000	63,601,000	20.22%	5,370,819	1.71%	8.44%
Oct-00	52,458,977	2,679,084,000	1.96%	328,773,000	68,048,000	20.70%	6,506,227	1.98%	9.56%
Nov-00	48,853,223	2,584,905,000	1.89%	320,934,000	65,170,000	20.31%	6,123,924	1.91%	9.40%
Dec-00	49,789,559	2,698,086,000	1.85%	336,786,000	62,758,000	18.63%	6,302,380	1.87%	10.04%
Jan-01	53,402,375	2,748,129,000	1.94%	344,333,000	65,164,000	18.92%	6,770,989	1.97%	10.39%
Feb-01	55,599,770	2,525,791,000	2.20%	315,854 000	59,195,000	18.74%	6,925,607	2.19%	11.70%
Mar-01	74,798,309	2,806,519,000	2.67%	348,761,000	64,909,000	18.61%	9,249,968	2.65%	14.25%
Apr-01	74,571,801	2,783,561,000	2.68%	345,033 000	62,423,000	18.09%	9,157,270	2.65%	14.67%
May-01	77,501,996	2,882,608,000	2.69%	353,451,000	64,709,000	18.31%	9,398,298	2.66%	14.52%
Jun-01	73,426,982	2,780,664,000	2.64%	339,196,000	59,512,000	17.55%	8,891,566	2.62%	14.94%
Jul-01	75,058,000	2,813,385,000	2.67%	343,772,000	63,300,000	18.41%	9,081,942	2.64%	14.35%
Aug-01	69,847,000	2,813,881,000	2.48%	344,134,000	65,266,000	18.97%	8,475,423	2.46%	12.99%
Sep-01	68,474,000	2,705,167,000	2.53%	333,702,000	62,512,000	18.73%	8,335,778	2.50%	13.33%
Oct-01	70,964,000	2,799,787,000	2.53%	348,227,000	67,376,000	19.35%	8,704,329	2.50%	12.92%
Nov-01	69,085,000	2,715,833,000	2.54%	340,431,090	64,513,000	18.95%	8,604,610	2.53%	13.34%
Dec-01	77,926,000	2,807,865,000	2.78%	355,814,883	63,555,843	17.86%	9,816,522	2.76%	15.45%
Jan-02	86,697,000	2,831,984,000	3.06%	359,196,648	66,261,752	18.45%	10,905,097	3.04%	16.46%
Feb-02	87,186,000	2,629,978,000	3.32%	332,093,444	60,238,737	18.14%	10,840,689	3.26%	18.00%
Mar-02	102,232,000	2,981,647,000	3.43%	374,657,114	65,135,499	17.39%	12,626,325	3.37%	19.38%
Apr-02	101,109,000	2,933,326,000	3.45%	364,794,785	64,325,532	17.63%	12,351,855	3.39%	19.20%
May-02	110,115,000	3,069,832,000	3.59%	381,861,433	66,946,643	17.53%	13,440,757	3.52%	20.08%
Jun-02									
Jul-02									
Aug-02									
Sep-02									
Oct-02									
Nov-02									
Dec-02									

*Jan 00 to June 00 O-O-S solids estimated using average of 12.34% solids as calculated using July 00-Dec 01 data.

Source: CDFA